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IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1944

No. 164-1165

LORRAINE CASTLE APARTMENTS BUILDING CORPORATION, INC., ET AL.,
Petitioners,

vs.

JUSTIN MACKIEWICH, ET AL.,
Respondents.

ANGELO CASTELLANI, ET AL.,
Petitioners,

vs.

JAMES W. McNICHOLS, TRUSTEE, ET AL.,
Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT WITH SUPPORTING BRIEF.

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Petitioners,

vs.

JAMES W. McNICHOLS, TRUSTEE, ET AL.,
Respondents.

PETITION.

To the Honorable, the Chief Justice and Associate Justices of the Supreme Court of the United States:

Lorraine Castle Apartments Building Corporation, Inc., Angelo Castellani, Margaret Castellani and Edward Gorman, pray that a Writ of Certiorari be issued to review the judgment of the United States Circuit Court of Appeals for the Seventh Circuit in the causes entitled: In the mat-

ter of Lorraine Castle Apartments Building Corporation, Inc., debtor; Lorraine Castle Apartments Building Corporation, et al, v. Mackiewich, et al, No. 8591, and Angelo Castellani, et al, v. McNichols, trustee, et al, No. 8597, affirming two orders of the District Court for the Northern District of Illinois, Eastern Division, in a reorganization proceeding under Chapter X of the Bankruptcy Act.

Summary Statement of Matters Involved.

In a voluntary proceeding for reorganization under Chapter X of the Bankruptcy Act the debtor sought an extension of time for payment of its bonds in full with interest or, in the alternative, immediate retirement of the bonds by borrowing as much as possible and making an additional contribution. In this way 80 cents on the dollar was assured to the bondholders, more than two-thirds of whom were willing to accept 80 cents on the dollar. The special master filed a report, of which no notice was given to the bondholders generally, recommending approval of debtor's plan of reorganization if bondholders received 85 cents on the dollar. Without informing bondholders of the report, speculators, one of whom had falsely stated to the special master that he represented a bondholder, solicited and bought up two-thirds of the bonds at less than 80 cents on the dollar for the purpose of preventing any reorganization and forcing a liquidation.

The District Court entered orders (1) denying a petition to restrict the claims of the speculators to the amounts they paid, and (2) approving a plan of "reorganization" providing for immediate liquidation, refusing to approve and submit the debtor's further proposal to contribute additional funds, make immediate distribution to bondholders of a substantial amount and pay the balance of

all claims in full in five years with interest at 5%, or, if such claims were so limited, to make immediate payment of all claims in full. The Circuit Court of Appeals affirmed both orders.

Opinions Below.

The opinion of the District Court for the Northern District of Illinois, Eastern Division, appears in the record at pages 446-451, and is reported in 42 Fed. Suppl. 973. The opinion of the Circuit Court of Appeals for the Seventh Circuit appears in the record at pages 495-502. The judgment of the Circuit Court of Appeals was entered on May 4, 1945 (R. 503). On May 16, 1945 an order was entered staying the issuance of mandates for a period of 45 days to enable petitioners to apply to this Court for the Writ of Certiorari (R. 505).

Jurisdiction.

The jurisdiction of this Court is invoked under Section 240 of the Judicial Code as amended. (28 U.S.C.A. 347.)

Questions Presented.

The questions presented by this petition for a writ of certiorari are:

1. While the Court in a Chapter X proceeding is in the process of working out a plan agreeable to the debtor and more than two-thirds of its creditors, is interference by speculators who connive and conspire to solicit and buy up more than two-thirds of debtor's bonds while the debtor's hands are tied, with the object of preventing reorganization and forcing liquidation, a violation of Chapter X of the Bankruptcy Act.

2. Under such circumstances should the Court have summarily denied the petition to restrict claims so purchased to the amount paid for them.

3. Under such circumstances should the Court have refused to submit to the creditors the debtor's proposal to contribute additional funds, make immediate distribution of a substantial amount, pay the balance of all claims in full in five years, with interest at 5%, or if such claims were so limited, to make immediate payment of all claims in full.

4. Under such circumstances does Chapter X of the Bankruptcy Act upon a voluntary petition for reorganization, permit liquidation under the guise of reorganization, without an adjudication in ordinary bankruptcy.

Reasons Relied Upon for the Allowance of the Writ of Certiorari.

I. The Circuit Court of Appeals for the Seventh Circuit has decided an important question of federal law which has not been, but should be, settled by this Court, namely: Is the solicitation by speculators of a debtor's bonds during the pendency of a reorganization proceeding under Chapter X of the Bankruptcy Act *for the purpose of preventing a reorganization* prohibited by the Act or general equitable principles, or is it to be sanctioned in order not to "destroy or impair the sales value of securities by abolishing the profit motive which inspires purchasers".

II. The Circuit Court of Appeals for the Seventh Circuit has decided a federal question in a way probably in conflict with an applicable decision of this Court, to-wit, *Fidelity Assurance Assn.* v. *Sims*, 318 U. S. 608, in which this Court said that "the statute does not contemplate a liquidation in a Chapter X proceeding, but a liquidation in ordinary bankruptcy, or a dismissal outright."

BRIEF IN SUPPORT OF PETITION FOR CERTIORARI

MAY IT PLEASE THE COURT:

Grounds on which jurisdiction of this Court is invoked are stated in the preceding petition, which also refers to the opinions below and contains a summary statement of the case.

Statement of Facts.

The debtor corporation was organized in 1928 (R. 174). Title to a twenty-six flat apartment building was conveyed to the corporation by Angelo Castellani and Margaret Castellani (R. 179), subject to a mortgage securing an indebtedness of $100,000, with interest at 6% per annum, maturing on May 1, 1935 (R. 149). The building was erected at the height of the building boom in 1928 by the Castellanis, whose personal investment was $48,000 (R. 155-204). On May 1, 1933, the bondholders voluntarily agreed to reduce the interest rate from 6% to 4% (R. 52). Prior to May, 1935, the outstanding balance of the indebtedness being $85,900.00, the debtor filed a petition under Section 77B pursuant to which a plan of reorganization was put into effect by which maturity was extended to May 1, 1942, with interest at 3% per annum, with sinking fund provisions (R. 52). Prior to the extended maturity and when the petition was filed herein, the indebtedness, by means of the sinking fund, had been reduced to $72,500.00 (R. 5). During operation of the 77B plan then in force all of the net income from the property, after payment of taxes and interest, had gone into the sinking fund for the retirement of bonds (R. 175, 177, 185, 204). The Castellanis never received anything from the operations,

except that Angelo Castellani, as provided in the plan, received a commission of 4% for operating the property. He paid full rental on the apartment occupied by him (R. 175).

The petition was approved as filed in good faith (R. 11), and referred to a special master (R. 12). At a hearing on May 13, 1942, it was represented to the special master by a bondholder that the majority of the bondholders felt that they would much rather have a settlement of from 75 to 80% than an extension (R. 172). The debtor filed a plan or reorganization (R. 21) providing for retirement of the bonds by the negotiation of a loan on the property in the amount of $40,000 (increased to $50,000) and that Angelo Castellani would borrow, on his personal credit, $10,000, enabling immediate payment to bondholders of 70% (increased to 80%) of the face value of their bonds, the debtor paying all loan commissions, current bills, costs and allowances made by the Court. At a hearing on this plan on September 10, 1942, the special master stated that in his opinion the fair cash market value of the property was $62,250.00 (R. 199).

The special master reported to the Court that "there is every indication that at least 85 per cent of the face value of the bonds can be realized by the owners and holders of first mortgage bonds at a liquidation sale of the property herein involved". No notice of this report was sent to the bondholders generally, who knew only of the debtor's original plan providing for 70 cents on the dollar. At this point speculators desiring to acquire the debtor's assets solicited and acquired bonds from the then holders at prices ranging from 70 to 77 cents on the dollar without advising the sellers of the special master's report.

Following the concentration in the hands of William Bart of the speculatively acquired bonds, Bart filed objections to the debtor's amended plan of reorganization and objections to the special master's supplemental report of January 16, 1943 in which the special master stated that if the debtor should increase its offer to pay bondholders 85 cents on the dollar he would recommend to the Court approval of such plan (R. 51, 67). The debtor suggested that if the claims of the speculators were allowed only in the amount of the actual cost of the bonds the debtor would present an amended plan whereby the speculators would receive the amount which they paid for their bonds and the remaining bondholders the face amount of their bonds (R. 84).

The District Court held the matter under advisement for seven months and then, without notice, application or hearing, ordered that the debtor be removed from possession of the property, appointed a trustee and directed him to file a plan involving liquidation. This the trustee did, the "plan" being liquidation.

The debtor, its stockholders and a bondholder on November 1, 1943, presented a motion requesting leave to file a petition praying for the entry of an order limiting the allowance of claims based on bonds purchased during the pendency of the proceedings to the amounts actually paid for them (R. 168, 450, 452-456). On February 10, 1944, the Court entered an order permitting the filing of the petition and denying it. The petition set forth the activities of the speculators in considerable detail, charged that they "formed a plan to acquire enough of the outstanding bonds of the debtor to control the reorganization sought by these proceedings, conspired to thwart the functioning of the Bankruptcy Act and to defraud the debtor, its stockholders and certain of its creditors" (R. 452-456).

The statement of the Circuit Court of Appeals for the Seventh Circuit in affirming the order denying this petition that "the record discloses that the court had already made an adjudication of the issues involved before this petition was filed" *is incorrect.* The District Judge heard no evidence at any time. No issue was ever drawn and prior to the denial of the petition to limit claims no adjudication was ever made of the questions raised thereby. After hearings on the first plan proposed by the debtor the special master reported that "confronted with the conflicting testimony and the evidence of manipulations, schemes and financial intrigue that have been manifested by persons who had busied themselves acquiring bonds during the pendency of these proceedings" he was reluctant to place any confidence in their assurances, but there was then no issue as to the claims based upon such purchases and *the report was never passed upon by the Court.*

Appeals were taken both from the order of February 10, 1943, denying the petition to limit claims, and from the order of February 21, 1944, approving the trustee's plan for immediate liquidation by sale of the debtor's assets and distribution of the proceeds. *No finding of insolvency was ever made and no order adjudging the debtor a bankrupt was ever entered.*

Errors Relied Upon.

(1) The Circuit Court of Appeals was in error in holding that interference by speculators who connived and conspired to solicit and buy up bonds while a plan of reorganization was being worked out in a proceeding under Chapter X of the Bankruptcy Act and while the debtor's hands were tied, with the object of preventing reorganization and forcing liquidation, did not constitute a violation of Chapter X of the Bankruptcy Act or the general principles of equity jurisprudence.

(2) The Circuit Court of Appeals for the Seventh Circuit erroneously held that the District Court properly denied, without a hearing, the petition to limit claims purchased by speculators during the pendency of the reorganization proceeding to the amounts paid for them.

(3) The Circuit Court of Appeals for the Seventh Circuit erred in affirming the order of the District Court refusing to submit to the creditors the debtor's proposal to contribute additional funds, distribute immediately a substantial amount and pay the balance of all claims in full in five years with interest at 5%, or if such claims were so limited, to make immediate payment of all claims in full.

(4) The Circuit Court of Appeals for the Seventh Circuit erroneously stated, contrary to the record and to the fact, that "the record discloses that the court had already made an adjudication of the issues involved before this petition was filed."

(5) The Circuit Court of Appeals for the Seventh Circuit erroneously held that under such circumstances Chapter X of the Bankruptcy Act upon a voluntary petition for reorganization permits liquidation under the guise of reorganization without an adjudication in ordinary bankruptcy.

Summary of the Argument.

Chapter X of the Bankruptcy Act was enacted to give the debtor and its creditors an opportunity to work out a plan of reorganization in order to avoid liquidation. While the court is in the process of working out a fair and feasible plan agreeable to the debtor and more than two-thirds of its creditors interference by speculators with no previous interest who, while the debtor's hands are tied, conspire and connive to solicit and buy up more than two-thirds of the debtor's bonds *at less than the holders can obtain*

from the debtor, with the object of thwarting the Act and forcing liquidation, is in violation of the Act and contrary to the principles of equity jurisprudence. These activities should not be encouraged and aided by the court but the claims so purchased should be limited to the consideration paid therefor. Under such circumstances the court should not refuse to submit to the bondholders a fair plan submitted by the debtor to contribute additional money, make immediate distribution to bondholders of a substantial amount, and pay the balance in full in five years with interest at 5%, or, if such claims are so limited, to make immediate payment of all claims in full. Under such circumstances Chapter X does not permit liquidation upon a voluntary petition for reorganization without an adjudication in ordinary bankruptcy and it does not contemplate liquidation under the guise of reorganization.

ARGUMENT.

In *Case* v. *Los Angeles Lumber Co.*, 308 U. S. 106, 124, this Court said that one of the purposes of Section 77B was to avoid the consequences to debtors and creditors of foreclosures, liquidations and forced sales with their drastic deflationary effects. After the parties are brought into the bankruptcy court the interest of all, creditors and debtor alike, are to be determined according to the principles of equity. It was not the intention of Congress to offer relief to speculators in equities. Here the speculators formulated a scheme the effect of which was not only to deprive the legitimate bondholders or original owners from receiving the actual value of their bonds, but particularly to defeat the approval by the court of any plan whereby the debtor might satisfy all of its creditors and have something left. Settled principles of equity should prevent these speculators from enforcing any claim for more than the amount paid, with interest and expenses.

Chapter X of the Bankruptcy Act requires the court to take pains to determine whether settled principles of equity may not disable the assignee of a claim acquired during the proceedings from receiving more than he paid therefor:

Section 612 of the United States Code provides that the judge may limit to the actual consideration paid therefor any claim acquired in the course of a proceeding by an attorney purporting to represent any creditor. In this case one Rubin, purporting to represent Bart in whose name

all of the speculatively acquired bonds were subsequently concentrated, sent telegrams personally soliciting bonds during the proceeding (R. 416, 417, 418, 233), and personally entered into a contract during the proceeding for the purchase of other bonds (R. 419).

Section 576 provides (italics ours) that "*no person* shall, without the consent of the court, *solicit* any acceptance, conditional or unconditional, of any plan or any *authority*, conditional or unconditional, to accept any plan, whether by proxy, *deposit*, power of attorney, or *otherwise*, until after the entry of an order approving such plan * * * "

Section 603 requires the judge in acting on a plan to investigate and consider the good faith and propriety of the acceptances and the time of acquiring the claims.

Section 610 prohibits an attorney from being heard until he has filed a statement with the court showing the time of acquisition of the claims represented by him.

Section 611 requires every person representing more than twelve creditors to file a statement reciting the facts and circumstances of his employment, the amount of the claims owned by him, the times when acquired and the amounts paid therefor.

Section 613 prohibits an agent of creditors from being heard until he has satisfied the court that he has complied with all applicable laws regulating the activities of such persons.

It was not contemplated by Congress that the very purpose of the Act and object of the proceeding should be thwarted by the purchase of claims during the proceedings and that the court should place its *imprimatur* upon "manipulations, schemes and financial intrigue that

have been manifested by the individuals who have busied themselves acquiring bonds during the pendency of these proceedings." (Special Master's report, R. 62.)

By its judgment affirming the order denying the petition of the debtor, its stockholders and a bondholder, without requiring an answer thereto, or a hearing, the Circuit Court of Appeals, in effect, has held that the petition was insufficient as a matter of law. This court, in *American Insurance Co.* v. *Avon Park,* 311 U. S. 138, 145, has plainly indicated that the court has ample power to deal with a situation involving unfair dealing, special benefits to a few, etc., to say nothing of a deliberate intent and plan to thwart the purpose of the Bankruptcy Act.

In determining that there should be a liquidation in this case and that it was not necessary that there be an adjudication in ordinary bankruptcy the District Court and the Circuit Court of Appeals considered that the statement of this Court in *Fidelity Assurance Assn.* v. *Sims,* 318 U. S. 608, was a mere dictum to be disregarded. In that case this Court said:

> "Under the predecessor of Chapter X—Section 77B of the Bankruptcy Act—the district judge was given authority by sub-section c (8), under certain circumstances, to 'direct the estate to be liquidated, or direct the trustee or trustees to liquidate the estate * * *.' In Chapter X on the other hand, section 236 (2) provides that if no plan is approved or accepted, or if it is not consummated, the judge may, after hearing all persons in interest, adjudge the debtor a bankrupt, or dismiss the proceeding as he may decide is in the interest of creditors and stockholders. Thus the statute does not contemplate a liquidation in a Chapter X proceeding but a liquidation in ordinary bankruptcy or a dismissal outright."

It is respectfully submitted that careful examination of the opinion of the District Court in that case (42 Fed. Sup. 973), the opinion of the Circuit Court of Appeals (129 Fed. 2d. 442), the petition for certiorari, and the briefs, plainly shows that the language of this court above quoted was not a mere *obiter dictum,* but that the question was actually presented and necessarily presented for the decision of this court.

Paragraph (2) of Rule LII of the Rules in Bankruptcy of this court provide that General Order in Bankruptcy No. XVIII, having to do with the sale of property, shall not apply to proceedings under Chapter X of the Act "unless an order shall be entered directing that bankruptcy be proceeded with pursuant to the provisions of the Act."

Under Section 616 a plan of *reorganization* may provide for a class of creditors which has not accepted a plan by the sale of property free of such claims and the transfer of the claims to the proceeds of such sale. However, Chapter X does not contemplate *liquidation* under this provision by calling it "reorganization".

Whether or not the court has the power, in a proper case, to approve a plan providing for the liquidation of a debtor's assets, such power should not be exercised when its exercise places the stamp of approval upon such activities as those disclosed by this record.

It is respectfully submitted that the Circuit Court of Appeals erroneously cast aside these considerations and principles in order not to "destroy or impair the sales value of securities by abolishing the profit motive which inspires purchasers."

WHEREFORE it is respectfully submitted that this petition should be granted.

LORRAINE CASTLE APARTMENTS BUILDING CORPORATION, INC.,
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EDWARD GORMAN,

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In the Supreme Court of the United States

OCTOBER TERM, 1945

NOS. 164 AND 165

LORRAINE CASTLE APARTMENTS BUILDING CORPORATION, INC., ET AL., PETITIONERS

v.

JUSTIN MACKIEWICH ET AL., AND THE SECURITIES AND EXCHANGE COMMISSION

ANGELO CASTELLANI ET AL., PETITIONERS

v.

JAMES W. MCNICHOLS, TRUSTEE, AND THE SECURITIES AND EXCHANGE COMMISSION AND WILLIAM BART

ON PETITION FOR WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT

BRIEF FOR THE SECURITIES AND EXCHANGE COMMISSION IN OPPOSITION

OPINIONS BELOW

The opinion of the District Court of the United States for the Northern District of Illinois, Eastern Division (R. 446–451) is reported in 53 F.

Supp. 994. The opinion of the Circuit Court of Appeals for the Seventh Circuit (R. 495–502) is reported in 149 F. 2d 55.

JURISDICTION

The judgments of the circuit court of appeals were entered on May 4, 1945 (R. 503–504). The petition for writs of certiorari was filed on June 25, 1945. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTIONS PRESENTED

1. Whether, in reorganization proceedings under Chapter X of the Bankruptcy Act, the district court properly granted full participation and voting rights to bonds purchased during the pendency of the proceedings, where there was no showing that the bonds were purchased for any motive other than profitable speculation, and there was no finding of fraud, breach of fiduciary relationship, or access to inside information by the purchasers.

2. Whether a district court, in a Chapter X proceeding, has the power to approve a plan of reorganization which provides for the sale of all of the debtor's property to outside interests at not less than a fair upset price.

STATUTE INVOLVED

The relevant provisions of the Bankruptcy Act are set forth in the Appendix, *infra*, pp. 18–20.

STATEMENT

The debtor, Lorraine Castle Apartments Building, Inc., owns and operates a small apartment building in Chicago and has outstanding $72,500 principal amount of first mortgage bonds secured by a trust deed covering the property, dated March 17, 1928 (R. 2–3, 35). All of the stock of the debtor corporation is owned by Angelo Castellani and Margaret Castellani, petitioners, and, until the appointment of the trustee, Angelo Castellani managed the property of the debtor (R. 4, 142).

Organized as an Illinois corporation in 1928, the debtor initially issued $100,000 principal amount of its first mortgage bonds, of which $85,900 were outstanding on May 1, 1935, the maturity date. A reorganization effected under Section 77B of the Bankruptcy Act at that time resulted in a plan whereby the maturity was extended seven years to May 1, 1942, interest was waived during the first year of the extended period and fixed thereafter at a reduced rate of 3% per annum until maturity, and the stock of the debtor was unaffected. (R. 21.)

In view of its inability to pay the $72,500 of bonds outstanding at the extended maturity date, the debtor, on April 30, 1942, filed a petition for reorganization under Chapter X of the Bankruptcy Act (R. 2–6). On May 5, 1942, the judge approved the petition as filed in good faith and left the debtor in possession of its property (R.

11) until July 20, 1943, when the judge appointed a trustee (R. 92). On July 22, 1943, the district judge requested the Securities and Exchange Commission to file its notice of appearance (R. 102–103), pursuant to Section 208 of the Bankruptcy Act (11 U. S. C. 608), and the Commission became a party to the proceedings.

On August 12, 1942, the debtor filed a plan of reorganization pursuant to which bondholders were to be paid 70% of the amount of their bonds in full settlement of their claim (R. 21–24). The plan was found by a special master to be inadequate in a report (R. 24–32) in which he indicated that at least 85% could be realized by sale of the property (R. 30). Thereafter, certain persons, apparently acting in part in concert (R. 56–61), acquired $52,000 in principal amount of the outstanding bonds for which they paid prices ranging from 70 to 90 cents on the dollar (R. 49, 38, 39); one William Bart, paying 90 cents on the dollar (R. 47, 264–269) became the owner of these bonds, and was thereafter granted leave to intervene (R. 47, 50, 51). None of the individuals who acquired the bonds was ever an officer or director of the debtor or connected with the indenture trustee and none of them had access to inside information (R. 161, 162). The district court affirmed the special master's finding that none of them occupied a fiduciary relationship and that no fraud had been practiced by them in acquiring the bonds (R. 64–65, 160, 449).

On July 20, 1943, the court ordered that the debtor be removed from possession of the property, appointed James W. McNichols trustee, and directed that he prepare a plan of reorganization embracing the sale of the property if fair and feasible and submit it to the special master (R. 92).

On August 31, 1943, the trustee filed a plan of reorganization which provided that the debtor's property be publicly offered for sale at an upset price of $75,000, that the proceeds of such sale, together with cash on hand after payment of expenses, be used to pay in full the claims of bondholders for principal and interest, and that the balance, if any, be paid to stockholders. This plan also provided that in the event of a failure to realize the upset price, a corporation should be formed to operate the property and own it free and clear of the mortgage; all the stock of such corporation would then be issued ratably to the bondholders. (R. 104–113.) The upset price in the trustee's plan was based upon the appraisal dated August 20, 1943, by Paul A. Hazard (R. 114–125). Subsequently the trustee received an offer from one Frank Heller to pay $75,000 for the property; this offer was accompanied by a deposit of $7,500 (R. 377, 388–389).

On September 15, 1943, the debtor submitted another plan (R. 138–141) under which 20% of the face amount of the bonds would be paid immediately and the rest in five years; the stock of

the debtor would be left unaffected. The special master found this plan unfair and not feasible (R. 162), but found the trustee's plan fair and feasible (R. 163). The district court approved the report of the special master (R. 446–451). It issued an order, on February 10, 1944, denying a petition (R. 452–456) to limit the participation of holders of bonds purchased while the proceedings were pending (R. 451), and, on February 21, 1944, entered an order approving the trustee's plan of reorganization (R. 457–460). On appeals from both orders (R. 461, 477),[1] the circuit court of appeals affirmed (R. 503, 504).

ARGUMENT

1. Contrary to petitioners' assertion (Pet. 8, 9), the character of those who purchased bonds while the Chapter X proceedings were pending was fully canvassed by the special master and, as the court below held (R. 499–500), no answer to the petition to limit the claims or hearing thereon was required. The petition was filed after the issue had already been before the special master, and his report that there was "no attempt * * * to perpetrate a fraud upon this Court" (R. 64), that there was no proof adduced to show that the purchasers "induced the bondholders to part with their bonds upon any false representations" (R.

[1] The appeal from the order dated February 10, 1944, was docketed in the court below as No. 8591; that from the order of February 21, 1944, was docketed as No. 8597.

160), and that these purchasers were entitled to participate fully, as provided in the trustee's plan (R. 158),[2] because there was no "privity" between them and the debtor (R. 161), was approved by the district court (R. 449). The evidence shows, and it is not denied by petitioners, that none of the purchasers was a fiduciary, dealt with fiduciaries, had access to inside information, or committed fraud in the conduct of their purchase transactions.

Consequently, it is clear that on a record which is devoid of any foundation for an equitable exception, the rule that holders of securities purchased prior to or during the pendency of reorganization proceedings are entitled, regardless of the prices at which the bonds were purchased, to participate on a parity with those persons who are original holders was properly invoked by the

[2] The objections of the Castellanis to the trustee's plan, filed September 15, 1943, recited *inter alia* (R. 143):

> Said speculators, holding said bonds in the aggregate face amount of Fifty-two Thousand Five Hundred Dollars ($52,500.00) are not entitled to have their claims allowed on a parity with other bondholders, but their claims should be limited to the amount paid for such bonds, being approximately Thirty-eight Thousand Dollars ($38,000.00). Such bondholders should be separately classified for the further reason that they are not entitled to vote on any plan.

Both before and after the filing of the objections to the trustee's plan, the question of limiting claims permeated the record and was the subject both of evidence and considerable colloquy (R. 217–312; 326–398).

court below. *Mokava Corporation* v. *Dolan,* 147 F. 2d 340 (C. C. A. 2); *Security-First Nat. Bank* v. *Rindge Land and Navigation Co.,* 85 F. 2d 557, 561, 563 (C. C. A. 9), certiorari denied, 299 U. S. 613; *Standard Gas & Electric Co.* v. *Deep Rock Oil Co.,* 117 F. 2d 615, 619 (C. C. A. 10), certiorari denied, 313 U. S. 564.

Section 212 of the Bankruptcy Act (Appendix, *infra,* p. 18), the so-called "scrutiny clause" of Chapter X, which provides that the court may limit to cost, claims or stock acquired in contemplation of or in the course of Chapter X proceedings by agents, attorneys, indenture trustees or committees is, as the court below held (R. 498), not applicable to third parties, to strangers to the proceedings, or to anyone who is under no fiduciary obligation to the corporate creditors or stockholders. Indeed, the imposition of any such limitation under the circumstances of this case would be against public policy in that it would "impair the sales value of securities" and "encourage the debtor to delay the plan for rehabilitation in the hope that he will be able to settle the claims against him at less than a fair amount" (R. 499).

Petitioners state that the speculative purchases of bonds during the proceedings were designed "for the purpose of preventing a reorganization" and "thwarting the Act and forcing liquidation" (Pet. 3, 4, 10). But the record contains no

evidence of any purpose on the part of those who purchased bonds of the debtor during the proceedings other than profitable speculation. They did nothing to prevent the debtor from putting through a plan providing for the continued operation of the debtor. On the contrary, it was the district judge and the trustee who were responsible for the submission of a plan providing for the sale of the property (R. 92, 104). Since there was no showing that the bonds in question were purchased for any motive other than profitable speculation, it would have been improper for the court to have disqualified the bonds from voting on the plan. And for reasons already stated, there was no basis in the record for limiting to cost, claims arising from the bonds.[3]

2. The circuit court of appeals properly held that the district court had the power, in this

[3] In the lower court and in their petition, the petitioners have not distinguished between limitation to cost and disqualification of voting rights—two separate problems. Cf. Sections 203 and 212 (Appendix, *infra*, p. 18). The purpose for which the bonds were purchased bears only on the question whether the bonds should be disqualified from voting, not on whether they should be limited to cost. See Section 203; Hearings on H. R. 6439, reintroduced and reported as H. R. 8046, before the House Committee on the Judiciary, 75th Cong., 1st Sess., pp. 180–182; *Young* v. *Higbee Company*, 324 U. S. 204, 211, note 10. Even when the vote of a claim is disqualified, the holder of the claim, in the absence of fraud, breach of fiduciary duty, or access to inside information, is entitled to participate on a parity with the holders of claims of the same class in whatever plan is confirmed.

Chapter X proceeding, to approve a plan providing for the sale of all of the debtor's property at not less than a fair upset price, and this decision, contrary to petitioners' allegation (Pet. 4, 13–14), does not conflict with *Fidelity Assurance Ass'n* v. *Sims*, 318 U. S. 608. Petitioners argue, in effect, that in order for a plan to be effectuated as a plan of reorganization under Chapter X of the Bankruptcy Act, it must contemplate the continued participation of some class of the debtor's securities in the operation of the debtor or a successor corporation as a going concern. But a plan providing for the sale of the debtor's principal assets and the distribution of the proceeds thereof together with the distribution of other assets, such as cash, among security holders and other claimants (R. 132–133) is expressly provided for by Section 216 (10) of the Act (Appendix, *infra*, pp. 18–19). Section 216 provides, in part, as follows:

> A plan of reorganization under this chapter—
>
> * * * * *
>
> (10) shall provide adequate means for the execution of the plan, which may include: the retention by the debtor of all or any part of its property; the sale or transfer of all or any part of its property to one or more other corporations theretofore organized or thereafter to be organized; the merger or consolidation of the debtor with one or more other corporations; the sale of

> all or any part of its property, either subject to or free from any lien, at not less than a fair upset price and the distribution of all or any assets, or the proceeds derived from the sale thereof, among those having an interest therein;

If a proposed plan of reorganization for a debtor which provides for "the sale of all * * * of its property * * * at not less than a fair upset price and the distribution of * * * the proceeds derived from the sale thereof, among those having an interest therein," may be characterized as a plan of liquidation, such a plan is nevertheless expressly authorized by the statute. In *Country Life Apartments, Inc.* v. *Buckley,* 145 F. 2d 935, 938, the Second Circuit adopted the same construction as that of the court below in the instant case. No other circuit has taken a contrary view. And even under the narrower provisions of former Section 77 B (b) (9),[4] a plan looking to the ultimate piecemeal liquidation of the debtor was upheld as a plan of reorganization. *In re Central Funding Corporation,* 75 F. 2d 256, 259 (C. C. A. 2). See also *Clinton Trust Co.* v. *John H. Elliott Leather Co.,* 132 F. 2d 299, 304 (C. C. A. 2).

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[4] Section 77B (b) provided in part:

> A plan of reorganization within the meaning of this section * * * (9) shall provide adequate means for the execution of the plan, which may include * * * the distribution of assets among creditors or any class thereof * * *

Fidelity Assurance Ass'n v. *Sims,* 318 U. S. 608, is not authority for the proposition that a Chapter X plan must provide for the continued operation of the debtor or a successor corporation as a going concern. The *Sims* case stands only for the proposition that a petition instituting proceedings under Chapter X must be dismissed for failure to meet the statutory requirement that a petition must be filed in good faith (Section 141, 11 U. S. C. 541) where it appears at the inception of the proceedings that the only possible accomplishment of the proceedings would be piecemeal liquidation as in an ordinary bankruptcy liquidation of a debtor.

In the present case, the petition was filed by the debtor in April 1942, was duly approved as properly filed in good faith, and no appeal was taken from the district court's findings. The debtor filed an original plan and subsequently an amended plan. It was not until almost a year and a half after the institution of the proceedings that the court appointed a trustee and directed him to file a plan providing for the sale of the property and the distribution of the proceeds. The court below properly stated that the only question involved in the *Sims* case was whether the petition was lacking in good faith and declared the holding of that case to be that the petition was not filed in good faith where "at the inception of the proceedings, it was obvious that

the only possible accomplishment would be piecemeal liquidation as in ordinary bankruptcy" (R. 500–501). Accord: *Country Life Apartments, Inc.* v. *Buckley,* 145 F. 2d 935, 938 (C. C. A. 2); *Patent Cereals* v. *Flynn,* decided June 7, 1945 (C. C. A. 2).

Where a sale plan is not the only type of plan which could be formulated, but is determined by the court to be fair, equitable, and feasible, and preferable to others submitted, it is clear from the express language of the statute that such a plan is permissible under Section 216 (10) of Chapter X.[5] Inexorable and inevitable piecemeal liquidation plainly foreseeable at the outset, which was the debtor's situation confronting the court in the *Sims* case, is quite different from the instant case. Here there were presented at the outset various possibilities as to plans of reorganization, and the particular plan involving a sale of the entire assets at not less than a fair upset price was selected by the court from these various possibilities.

[5] As the below court stated (R. 501–502), Section 236 of the Act (Appendix, *infra*, pp. 19–20) is applicable only where a plan of reorganization *within the meaning of Section 216* cannot be effectuated because no such plan is proposed, or a proposed plan is not approved by the judge, or an approved plan is not accepted, or confirmation is refused, or a confirmed plan is not consummated. In other words, the judge must resort to Section 236 where those having an interest in the debtor cannot achieve the cooperation necessary to effectuate a fair, equitable, and feasible plan within the scope of Section 216.

The construction of Section 216 (10) adopted by the court below is consistent with the flexibility of remedies inherent in the reorganization court as a court of equity.[6] The existence of the possibility of a plan of sale under Section 216 (10) is important to prevent debtors from abusing their right to file petitions under Chapter X in circumstances where there is no reason for a court to find at the outset a lack of good faith. In this case, the debtor had procured in 1935 a seven-year extension of the debt and a reduction of the interest rate in proceedings under Section 77B. The debtor's original purpose in filing the Chapter X petition was merely to get a further extension. When it was pointed out that the bondholders, many of them of advanced age, had waited long enough for payment (R. 29), the debtor filed a plan providing for the payment of 70% of the face amount of the bonds in full settlement of the bondholders' claims. After the special master stated that he could not approve the payment of less than 85% of the face amount, the debtor offered to pay 80% of the face amount. Finally, after the proceedings had been pending

[6] The Congressional intent to give the reorganization court broad powers to protect the interests of security holders appears also from Section 116 (3) (11 U. S. C. 516 (3)). To meet the situations of great urgency, that Section gives the court power to authorize the trustee to sell the property of the debtor, upon cause being shown, even without a plan being filed or an appraisal being made. *In re V. Loewer's Gambrinus Brewery Co.*, 141 F. 2d 747, 749 (C. C. A. 2).

for almost eighteen months and the trustee had proposed a plan which would result in the bondholders being paid 100% of their claim, the debtor's best offer was the immediate payment of approximately 20% of the principal with a five-year extension of the balance, a plan which the district court found unfair and not feasible.[7]

Under the circumstances, approval of the trustee's plan was in the interest of the requirements of fairness and equity. Certainly the alternatives afforded by Section 236 were undesirable. Dismissal of the proceedings would have been grossly inequitable to the bondholders who have had to wait nine years without payment. They would then have been relegated to their remedy of foreclosure with its inherent delay and expense after already having incurred the delay and expense of Chapter X proceedings which were instituted by the debtor. The other alternative was an adjudication of bankruptcy. And in such case it is by no means clear that the bankruptcy court would have jurisdiction over the assets or that the bond-

[7] In their petition (pp. 4, 9), petitioners raise the question whether it was error for the district court to refuse to submit the debtor's proposal to the security holders. Since it is clear that the proposal was unfair in requiring bondholders to extend the maturity of their bonds without compensation, and was not feasible because the financial condition of the debtor was such that another reorganization might well have been necessary (R. 448, 502), the district court was obviously correct in refusing to submit the proposal.

holders could participate in the proceedings. See Sections 56 (b), 57 (e), 57 (h) and 70 (a) (11 U. S. C. 92 (b), 93 (e), 93 (h), and 110 (a). For the normal rule in bankruptcy is that a bankruptcy court has control over properties which are security for obligations of a bankrupt only to the extent necessary to protect the rights of other security holders who may have an interest in the security after the secured creditors are satisfied. *Isaacs* v. *Hobbs Tie & Timber Co.*, 282 U. S. 734, 738.[8] But even if liquidation in straight bankruptcy were legally permissible, such a liquidation is by no means the same as a sale pursuant to Section 216 (10) under a plan. A plan of reorganization must provide that sale of the property shall be at not less than a fair upset price. A liquidation in bankruptcy may or may not be pursuant to a sale at an upset price. Furthermore, under Chapter X there is always available the alternative of substituting a plan providing for the operation of the property by a reorganized company if no bid equal to the upset price is received. The consequent greater independence of a trustee under Chapter X is apt to bring

[8] In the present case, with the possible exception of a current tax claim, there are no claims against the debtor, other than the secured bonds (R. 131). Consequently, it seems unlikely that the bankruptcy court would have any interest in the sale of the property unless there was a showing of a substantial equity which might be lost by foreclosure. And such a showing does not seem probable.

larger proceeds than a sale in bankruptcy or foreclosure which is made at whatever price the assets will bring.*

Thus, the lower court's construction of Section 216 (10) is not only in accordance with the plain meaning of the words used therein but also is consistent with the requirements of fairness and equity.

CONCLUSION

The decision of the court below is correct and there is no conflict of decisions. Consequently, the petition for writs of certiorari should be denied.

Respectfully submitted. HAROLD JUDSON,

Acting Solicitor General.

ROGER S. FOSTER,
Solicitor,
Securities and Exchange Commission.

JULY 1945.

* Somewhat the same advantages may perhaps be attained by a court in straight bankruptcy. Thus, if no adequate bid is received in a bankruptcy sale, the court might refuse the bid and dismiss the proceedings in order to permit new proceedings under Chapter X to be commenced. However, there is no need for such a cumbersome procedure where the company is already under Chapter X.

APPENDIX

The pertinent provisions of Chapter X of the Bankruptcy Act, c. 575, 52 Stat. 883, 11 U. S. C. 501, *et seq.*, are as follows:

> SEC. 203. If the acceptance or failure to accept a plan by the holder of any claim or stock is not in good faith, in the light of or irrespective of the time of acquisition thereof, the judge may, after hearing upon notice, direct that such claim or stock be disqualified for the purpose of determining the requisite majority for the acceptance of a plan.
>
> * * * * *
>
> SEC. 212. The judge may examine and disregard any provision of a deposit agreement, proxy, power or warrant of attorney, trust mortgage, trust indenture, or deed of trust, or committee or other authorization, by the terms of which an agent, attorney, indenture trustee, or committee purports to represent any creditor or stockholder, may enforce an accounting thereunder, may restrain the exercise of any power which he finds to be unfair or not consistent with public policy and may limit any claim or stock acquired by such person or committee in contemplation or in the course of the proceeding under this chapter to the actual consideration paid therefor.
>
> * * * * *
>
> SEC. 216. A plan of reorganization under this chapter— * * *
>
> (10) shall provide adequate means for the execution of the plan, which may in-

clude: the retention by the debtor of all or any part of its property; the sale or transfer of all or any part of its property to one or more other corporations theretofore organized or thereafter to be organized; the merger or consolidation of the debtor with one or more other corporations; the sale of all or any part of its property, either subject to or free from any lien, at not less than a fair upset price and the distribution of all of any assets, or the proceeds derived from the sale thereof, among those having an interest therein; the satisfaction or modification of liens; the cancellation or modification of indentures or of other similar instruments; the curing or waiver of defaults; the extension of maturity dates and changes in interest rates and other terms of outstanding securities; the amendment of the charter of the debtor; the issuance of securities of the debtor or such other corporations for cash, for property, in exchange for existing securities, in satisfaction of claims or stock or for other appropriate purposes;

* * * * *

SEC. 236. If no plan is proposed within the time fixed or extended by the judge, or if no plan proposed is approved by the judge and no further time is granted for the proposal of a plan, or if no plan approved by the judge is accepted within the time fixed or extended by the judge, or if confirmation of the plan is refused, or if a confirmed plan is not consummated, the judge shall—

(1) where the petition was filed under section 127 of this Act, enter an order dismissing the proceeding under this chapter and directing that the bankruptcy

be proceeded with pursuant to the provisions of this Act; or

(2) where the petition was filed under section 128 of this Act, after hearing upon notice to the debtor, stockholders, creditors, indenture trustees, and such other persons as the judge may designate, enter an order either adjudging the debtor a bankrupt and directing that bankruptcy be proceeded with pursuant to the provisions of this Act, or dismissing the proceeding under this chapter, as in the opinion of the judge may be in the interests of the creditors and stockholders.

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CHARLES ELMORE CROPLEY

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1944

NOS. 8591 AND 8597

LORRAINE CASTLE APARTMENTS BUILDING CORPORATION, INC., *et al.*,

Petitioners,

vs.

JUSTIN MACKIEWICH, *et al.*,

Respondents.

ANGELO CASTELLANI, *et al.*,

Petitioners,

vs.

JAMES W. McNICHOLS, TRUSTEE, *et al.*,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT.

BRIEF OF JAMES W. McNICHOLS, TRUSTEE IN OPPOSITION.

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BRIEF OF JAMES W. McNICHOLS, TRUSTEE IN OPPOSITION.

REPORT OF OPINION IN CIRCUIT COURT OF APPEALS.

The opinion of the Circuit Court of Appeals is set forth in full at pages 495 to 502 of the printed record. We shall refer to the opinion as it appears in the printed record.

STATEMENT OF FACTS.

We wish to concisely present only those facts which we consider necessary and pertinent. The original mortgage secured by the property owned by the Debtor corporation herein was $100,000.00, with interest at 6% per annum, maturing May 1, 1935. This amount had been reduced under a Section 77-B Reorganization and retirement of bonds to $72,500.00 with interest at 3% per annum as of April 7, 1942. On April 30, 1942, the Debtor corporation instituted these proceedings (R. 2-10) and an order was entered upon said petition finding that the same was filed in good faith and in compliance with the Act of Congress (R. 11-14). The matter was referred to a Special Master for hearing (R. 12). The Debtor corporation filed its first Plan of Reorganization on August 12, 1942 (R. 21-24) providing for retirement of bonds and payment to the bondholders of 70c on the dollar. After numerous hearings, the Special Master filed his report on October 6, 1942, recommending the disapproval of the Debtor's Plan of Reorganization as submitted and stated that there existed a buyer who was offering approximately $2,250.00 more for the Debtor's property than was being offered by the Debtor itself in full satisfaction of the outstanding indebtedness (R. 24-32) and the Special Master stated that unless the Debtor increased its offer to pay the bondholders 85c on the dollar he would recommend a liquidation (R. 29-30).

After this statement was made on November 24, 1942, Ward Farnsworth, a well-known real estate appraiser, appraised the property as having a value of $61,000.00 and the Debtor corporation then filed its petition for leave to amend the Plan of Reorganization increasing the proposed payment to the bondholders from 70c to 80c on the

dollar as their respective distributive share (R. 33). On December 17, 1942, the Special Master reiterated his statement that the distribution to the bondholders should be at least 85c on the dollar of the face amount of the bonds before he would approve a Plan of Reorganization, and further stated that in his opinion an offer of 80c on the dollar is not sufficient (R. 47-52). The Debtor at that time suggested to the Court that the claims of the so-called speculators should be limited to their actual purchase price of the respective bonds which they had acquired (R. 84). On May 13, 1943, Appraisal Associates, Inc., filed its report and appraisal evaluating the property of the Debtor at $73,250.00 (R. 93-101). On September 1, 1943, Paul A. Hazard, an appraiser appointed by the District Judge, filed his report and appraisal, stating that the present cash market value of the Debtor's property was $75,000.00 (R. 114-125). Thereafter on September 7, 1943, James W. McNichols, the duly appointed and qualified acting Trustee, submitted and proposed the Trustee's Plan of Reorganization, which fixed a minimum sale price of $75,000.00 and proposed a reorganization and sale with an upset price pursuant to the provisions of Section 216(10) of Chapter X of the Bankruptcy Act as amended (R. 126-130).

On November 1, 1943, the Debtor, its stockholders and bondholders, presented a motion for leave to file a petition praying for an order limiting the allowance of claims of bondholders who purchased securities during the pendency of these proceedings and requesting that their claims be limited to the amounts of the respective purchase prices actually paid (R. 168, 450, 452-456).

The Special Master in his report of October 7, 1943, recommended approval of the Trustee's Plan of Reorganization (R. 158) and stated that he had been advised that

the Trustee had received an offer of purchase for the Debtor's property in the amount of $75,000.00, accompanied by a cashier's check of $7,500.00, as earnest money upon a contract for the purchase of the Debtor's property. The prospective purchasers were procured by a real estate broker and were not acquainted with any of the parties to the litigation.

While the record contains many pages of testimony by Nelson Anderson, William Bart, Irving Greenfield, Justin Mackiewich, William Henning Rubin, Charles Turner, Frank Wallach, and others, before the Special Master, and both the testimony and evidence submitted dealt with the activity of the so-called speculators in purchasing bonds during the pendency of these proceedings, the Special Master found that there was no fraud involved in the purchase of these bonds, and that the purchasers are not and never were in a fiduciary relationship with the bondholders, the Debtor, stockholders of the Debtor (R. 160-161). Examination of the lengthy and exhaustive hearings as shown by the record well demonstrates that the petitioner was given ample opportunity to present all matters pertaining to this issue but that the evidence, as presented, did not support a finding of fraud, collusion and that no fiduciary relationship existed (R. 498).

The Special Master also recommended that the Plan of Reorganization filed by the Debtor lacked feasibility and should be disapproved; that the objections filed by the Debtor to the Trustee's Plan of Reorganization be overruled (R. 161-163). Objections to the Referee's Report were filed on October 12, 1943.

Thereafter, on February 10, 1944, the District Judge filed a memorandum opinion (R. 446-451) finding that the Debtor's Plan was unfair and not feasible; that the Trus-

tee's Plan was fair and feasible; that the evidence in the case did not warrant disturbing the findings of the Special Master; that there was no fraud involved in the purchase of the bonds during the pendency of this proceeding, and that the purchasers were not in a fiduciary relationship with the bondholders, the Debtor, or stockholders of the Debtor. The Court also entered an order granting the Debtor leave to file its petition for allowance and limitation of certain claims and denied said petition (R. 452-456). On February 21, 1944, the District Judge entered an order approving the Special Master's Report approving the Trustee's Plan of Reorganization as fair, equitable and feasible and disapproving the Debtor's proposed Amended Plan (R. 457-460). From these last orders Angelo Castellani and Margaret Castellani perfected an appeal to the Circuit Court of Appeals (R. 461) (R. 477) and thereafter on May 4, 1945, the Circuit Court of Appeals for the 7th Circuit affirmed the orders entered by the District Court (R. 495-502). It is upon this record that a Writ of Certiorari is sought.

ARGUMENT.

A.

Chapter X Of The Bankruptcy Act Specifically Authorizes A Reorganization Of The Debtor By A Sale Of The Debtor's Assets At A Fair Upset Price As A Reorganization And Not A Liquidation.

Petitioners again contend that the present Plan of Reorganization is not a reorganization but a liquidation since it tends to deprive the holders of Debtor's securities from continued participation in the Debtor or the Debtor's successor corporation. This argument has been refuted before the District Court and the Circuit Court of Appeals; we shall again demonstrate the fallacy in Petitioner's position.

The District Judge's approval of the Trustee's Plan of Reorganization and the disapproval of the Debtor's Amended Plan of Reorganization was in conformity with the provisions of Chapter X of the Bankruptcy Act as amended and was proper. This position was affirmed by the Circuit Court of Appeals (R. 495-502).

On April 30, 1942 the Debtor corporation filed its petition (R. 2-10) and an order was entered upon said petition finding that the same was filed in good faith and in compliance with the Act of Congress (R. 11-14). After the Special Master duly considered the Plan of Reorganization as filed by the Debtor and recommended its disapproval and after the Debtor amended its Plan of Reorganization and subsequently filed its amended Plan, the District Judge appointed a Trustee who submitted the Trustee's Plan of Reorganization which was approved as amended (R. 457-460).

On September 1, 1943, Paul Hazard, an Appraiser appointed by the District Judge, filed an appraisal report in which he set forth that the present cash market value of the Debtor's lands and buildings was $75,000.00. The Trustee's Plan of Reorganization, as approved, provided that the Special Master shall offer the Debtor's property for sale to the highest bidder with an upset price of $75,000.00.

It should be noted in passing that the first Plan of Reorganization submitted by the Debtor corporation on August 12, 1942, (R. 21-24) provided for payment to the bondholders of only 70c on the dollar. On October 6, 1942, the Special Master stated that a buyer had offered $9,250.00 more than was offered by the Debtor for the property (R. 29). In recommending that the Debtor's Plan be disapproved, the Special Master stated:

> "There is every indication that at least 85% of the face value of the bonds can be realized * * * and unless the Debtor's offer is increased so as to pay the bondholders 85c on the dollar of the face value of their bonds I would respectfully recommend that an order of liquidation be entered and the property sold in accordance with the provisions of the Bankruptcy Act made and provided (R. 30)."

The Debtor, in spite of this statement by the Special Master, did not increase its offer to 85c on the dollar but instead filed a petition for leave to amend the Debtor's Plan of Reorganization to increase payment to the bondholders from 70c to 80c on the dollar (R. 33). At no time did the Debtor see fit to increase its offer to the respective bondholders in accordance with the increased valuation of the property, and in fact refused to do so (R. 202).

The District Judge has the authority in a Chapter X proceeding to approve a plan providing for the sale of all

of the Debtor's property at not less than a fair upset price. This is specifically provided for in Section 216(10) (11 U. S. C. Sec. 616(10)) of the Act.

Section 216(10) provides in part as follows:

> "A Plan of Reorganization under this Chapter * * * (10) shall provide adequate means for the execution of the Plan which may include the retention by the Debtor of all or any part of its property; *the sale of all or any part of its property, either subject to or free from any lien, at not less than a fair upset price* and the distribution of all or any assets, or proceeds derived from the sale thereof, among those having an interest therein." (Italics ours.)

The language is clear and explicit. There can be no doubt that the framers of this section and Congress clearly authorized and intended the Court to approve sales with an upset price and approve a Plan of Reorganization containing provisions for an upset price sale as a Plan of Reorganization and not in the nature of a liquidation.

A recent case which raised the same issues and which confirmed the position taken by the District Court under Section 216(10) is *Country Life Apartments* v. *Buckley,* 145 Fed. 2d, 935 (C. C. A. 2nd, Dec. 1944). In this case the Circuit Court of Appeals affirmed the District Court in approving a Plan of Reorganization with an upset price sale of $525,000.00 which was found to be the fair value of the Debtor's property. The Court found that the Trustee's Plan of Reorganization with an upset price sale was properly within the language of Section 216(10) of Chapter X, that this suit is not a liquidation of Debtor's property and distinguished between the case before it and *Fidelity Association* v. *Sims,* 318 U. S. 608, 67 Sup. Ct. 807 when it held:

"Appellants also contend that the trustee's plan could not be confirmed in reorganization proceedings, because it was in reality not a plan of reorganization, but only a means of effecting the complete liquidation of the debtor's property, within the condemnation of *Fidelity Assurance Ass'n* v. *Sims,* 318 U. S. 608, 63 S. Ct. 807, 87 L. Ed. 1032. That case, however, held merely that a petition is not filed in good faith where liquidation, and not a readjustment of the rights of creditors, was at the very outset the only outcome to be expected. There the petition was attacked for lack of good faith in the initial stages of the proceeding, and the Court held that a proceeding could not be instituted under Chapter X where there was no chance of reorganization. Here when the petition was filed it did not appear that the debtor had no chance for reorganization or that reorganization would not be a reasonable method of serving the best interests of creditors and stockholders. The District Court found that the petition was filed in good faith, and that order was never appealed from. It cannot now be attacked for lack of jurisdiction. Bankruptcy Act, §149. The course of proceedings indicates also the good faith of the attempts to reorganize. One plan, indeed, was well on its way to being made effective as early as 1942. Only because of the completion of the buildings and the refinancing of the corporate indebtedness during the course of administration did liquidation become the more desirable method of winding up the debtor's estate.

"Under these circumstances *Fidelity Assurance Ass'n* v. *Sims, supra,* does not apply, and the trustee's plan was properly approved and confirmed by the District Court as being within the language of Bankruptcy Act §216(10), which provides that a plan of reorganization may include the sale of all or any part of the debtor's property at a fair upset price and the distribution of all or any assets among those having an interest therein. This conclusion is amply supported by our own decisions and those of other courts."

In support of its finding and conclusion the Court cited *V. Loewers Gambrinus Brewery Co.*, 141 Fed. 2d, 747, (2d Cir.); *Lorraine Castle Apartments Building Corp.*, (D. C. N. D. Ill.) 53 Fed. Cir. 994; *Central Sounding Corp.*, 75 Fed. 2d, 256, (2d, Cir.); *Porto Rican American Tobacco Co.*, 112 Fed. 2d, 665 (C. C. A. 2d).

It was only after these proceedings had been pending for almost eighteen months and the Debtor's best offer was payment of approximately 20% of the principal with a five-year extension of the balance on a total payment of 80% to the respective bondholders, that the Trustee who was appointed proposed a Plan which would result in payment to the bondholders of 100% of their claims. Thus it is apparent, and the Circuit Court of Appeals so found, that the approval of the Trustee's Plan and the disapproval of the Plans filed by the Debtor was in the best interests and requirements of fairness and equity and that the District Judge was acting within his authority and power as set forth by the statutes and the interpreting decisions in approving the Trustee's Plan of Reorganization.

B.

The District Court Properly Refused To Limit The Claims Of Holders Of Bonds Purchased During The Pendency Of The Proceedings Or Limit Their Voting Rights.

Petitioners have raised several objections with reference to the so-called speculators but have not clarified their position regarding the issues raised. The question has two distinct issues: should the holders who acquired bonds during the pendency of these proceedings be disqualified from voting upon the Plan of Reorganization; and/or be limited in the amount of their respective claims and be prevented from participating on a parity with the other bondholders.

1. The findings of fact entered by the District Court were reviewed and sustained by the Circuit Court of Appeals:

After a full and complete hearing on all of the matters presented before him, the Special Master found that there was no fraud involved in the purchase of these bonds and that the purchasers are not and never were in a fiduciary relationship with the bondholders, the Debtor, or stockholders of the Debtor.

It should also be noted that the Securities and Exchange Commission actively participated in these proceedings since July 22, 1943. The Commission, which is ever alert in matters of questionable ownership or purchase of securities, has taken the position and stated to the Court that there is no legal basis or justification for disqualifying the purchasers or disallowing or limiting their claims (R. 407). The Commission's position remained the same during the entire proceedings, including oral argument before the Circuit Court of Appeals.

On November 1, 1943, Petitioners presented a petition to the District Court to limit claims (R. 452-456). The Court considered this petition and the entire record before it and on February 18, 1944, entered an order granting leave to file a petition instanter and denied the prayer thereof (R. 451). On February 10, 1944, the District Judge, William J. Campbell, entered a memorandum of opinion in which he found (R. 446-451):

> "With reference to the acquisition of $52,000.00 bonds by speculators during the pendency of the proceedings, the Special Master has found that there was no fraud involved in the purchase of these bonds and that the purchasers are not and never were in a fiduciary relationship with the bondholders, the Debtor, or stockholders of the Debtor. The evidence in this case does not warrant disturbing the finding of the Special

Master on these two points, and, *as there is no proof that the bonds in question have been acquired by their present owners for the purpose of accepting or rejecting a Plan other than in good faith, this Court is not disposed to disqualify these bonds from voting* upon the Plan of Reorganization approved herein. *Sections 203 of Chapter X of the Bankruptcy Act;* In re *Pine Hill Colleiries Co.*, 46 Fed. Supp. 669, 671 (D. C. E. D. Pa., 1942; *Texas Hotel Securities Corp.* v. *Waco Development Co.*, 87 F. (2d) 395, 398 (C. C. A. 5th, 1937).

> "*Under the facts of this case, there is no occasion to limit participation in a plan by the holders of bonds purchased during the pendency of these proceedings to the amount of their cost.* In re *Utilities Power & Light Corporation*, 29 Fed. Supp. 763, 770 (D. C. N. D. Ill., 1939); In re *Celotex Co.*, 12 Fed. Supp. 1, 5 (D. C. Del., 1935); In re *Indiana Central Telephone Co.*, 24 Fed. Supp. 342, 344 (D. C. Del., 1938); *In the matter of Point Land Company*, 37 A. B. R. (N. S. 464, 466 (D. C. W. P. Pa., 1937))." (Italics ours.)

and entered an order approving the Trustee's Plan of Reorganization (R. 457-460).

The weight and consideration to be given to findings of fact, which in this particular case was the specific finding of fact that each of the above named individuals is not and never was in a fiduciary relationship with the bondholders is clearly set forth in Rule 52(a) of the Civil Rules of Procedure:

> "findings of fact shall not be set aside unless clearly erroneous and due regard should be given to the opportunity of the trial court to judge the credibility of the witnesses. The findings of a Master to the extent that the Court adopts them shall be considered as the findings of the Court."

There are numerous cases which support this ruling.

Cleo Syrup Corporation v. *Coca Cola Co.*, 139 Fed. 2nd, 416, 417, (C. C. A. 8th, 1943); *Webb* v. *Frisch*, 111 Fed. 2d 887 (C. C. A. 7th, 1940); *District of Columbia* v. *Pace*, 320 U. S. 698, 701, 88 L. Ed. 408, 410.

Prior to the adoption of the Rules of Civil Procedure the same rule prevailed.

In *Adamson* v. *Gilliland*, 242 U. S. 350 (1917), Mr. Justice Holmes said on page 353:

> "* * * the case is preeminently one for the application of the practical rule that so far as the finding of the Master or Judge who saw the witnesses, depends upon the conflicting testimony or upon credibility of witnesses or so far as there is any testimony consistent with finding, it must be treated as unassailable."

Petitioners do not and cannot contend that the record contains no evidence to support the findings of the Special Master and the District Court, which has been affirmed by the Circuit Court of Appeals. These findings should be given their full legal consideration.

2. As to the disqualification from voting.

Section 203 provides that if the acceptance or failure to accept a Plan by holders of any claim is not in good faith irrespective of the time of acquisition thereof, the Judge, after hearing, may direct that the vote of this claim be disqualified. The purpose of this section is to prevent creditors from participating, who by use of obstructive tactics and holdup technique exact for themselves undue advantages from the other stockholders who are cooperating. Bad faith is to be attributed to claimants who opposed a plan for a time until they were "bought off"; those who refused to vote in favor of a plan (notes 9 and 10 on Page

598, *Young* v. *Higbee,* 63 Sup. Ct. 594). However, even when a claim is disqualified the holder is entitled to participate on a parity with the holders of claims of a similar class in absence of fraud, breach of fiduciary or access to inside information.

After an examination of the present record, it is apparent that the sole purpose of the various purchasers was to make a profitable speculation, and that they did nothing to prevent, frustrate, interfere with or obstruct a plan of reorganization providing for the continued operation of the Debtor. As the Court stated there was no proof that the bonds in question have been acquired by their present owners for the purpose of accepting or rejecting a plan other than in good faith and for this reason there is no showing that the bonds in question should be disqualified from voting on the plan (R. 450-1). *Young* v. *Higbee Co.,* 65 Sup. Ct. 594, p. 598-599 (Feb. 1945), supports the position taken by the District Judge.

3. As to limiting claims in participation and amount.

As to the limitation of the amount of claims, the evidence amply demonstrates that the various individuals who purchased bonds during the pendency of the proceedings were complete strangers to the Debtor (R. 498). None of the purchasers were fiduciaries, or dealt with a fiduciary, or had access to inside information.

As a general rule, the holder of an obligation is entitled to recover from the maker the entire extent of the maker's promise to pay. The mere fact that the holders of bonds may have purchased them at less than par does not affect their rights (R. 488-489). In re *Utilities Light & Power Corp.,* 29 Fed. Supp. 763, 770. Again, "in absence of fraud the prices which security holders pay for their securities do not affect the measure of their participation under the Plan of Reorganization," *Standard Gas & Elec.* v. *Deep*

Rock Oil Co., 117 Fed. 2d, 615, 619. Sec. 212 of Chapter X which provides that the Judge may limit its costs, claims, or stock acquired in contemplation of or in the course of Chapter X proceedings by attorneys or Trustees, does not apply to strangers to the proceedings (R. 498).

The Special Master found that there was no fraud involved in the purchase of $52,000.00 worth of bonds by outsiders during the pendency of the proceedings and that the purchasers were not in fiduciary relationship with the bondholders, Debtor or stockholders of the Debtor. This finding was adopted by the District Judge (R. 446-451) and by the Circuit Court of Appeals:

> "These provisions are not applicable to third parties, to strangers, or to anyone who is under no fiduciary obligation toward any beneficiary of the trust." (R. 498),

and again:

> "Indeed the evidence offered by the debtor and its stockholders failed utterly to establish any possible fraud upon the corporation or any of the beneficiaries of the estate" (R. 498).

Consideration should also be given to the financial chaos which would result if purchasers of securities during the pendency of protracted proceedings of a corporate reorganization would be limited to the actual cost or purchase price of the various securities. This would not only encourage the Debtor in each instance to delay and prolong proposals for rehabilitation or reorganization of the Debtor in order to procure the Debtor's obligations at lesser amounts, but would also prejudice and hamper the negotiability and transferability of all securities. The only logical conclusion of the Debtor's request and the Debtor's conduct throughout these proceedings is that it was desirous of squeezing the bondholders and availing itself of Court reorganization procedure in order to prevent the respective bondholders

from realizing full value on their bonds, all to the particular pecuniary benefit of the Debtor itself. Petitioner undoubtedly is familiar with the decisions and legal principles set forth in *Case* v. *Los Angeles Lumber,* 308 U. S. 106, 60 Sup. Ct. 1.; *Consolidated Rock Products Co.,* 311 U. S. 636; *Northern Pacific Railroad Co.,* v. *Boyd,* 228 U. S. 482, in which the Court held that the owner of the equity is precluded from receiving an interest in the Debtor or its estate until such time as the prior liens are paid in full according to the terms and priority of the respective obligations.

A most pertinent case on this subject is *Mokova Corp.* v. *Dolan,* 147 Fed. 2nd, 340 (C. C. A. 2d, Jan. 1945), in which the Court stated on page 344-45:

> "Nor is it relevant that Meyer paid 50 or less for the second mortgage bonds he held. To reduce a creditors participation in the plan to the amount he paid for his bonds (except in unusual circumstances not present here) would be harmfully to reduce the value of such bonds to those who previously owned them."

There was no finding of fraud, breach of fiduciary relationship or access to information not publicly disclosed, on the part of the holders of the respective bonds so as to prevent their participation on a parity with the other bondholders. For the reasons herein contained these bondholders should not be disqualified from either voting or participating in the Plan on a parity with the other bondholders.

CONCLUSION.

As is ably said in the Opinion of the Circuit Court of Appeals, affirming the District Court:

> "Considering this picture as a whole and the findings of fact made by the Court in pursuance of the Special Master's recommendations, we cannot say that the ap-

proval of the trustee's plan was not in compliance with the Act of Congress or in the interest of fairness and equity (R. 502)."

It is apparent from the Opinion that the Court was familiar with the record and the issues. We submit that this statement is a considered opinion. The evidence and issues in this case have been thoroughly weighed by the Special Master, the District Court and the Circuit Court of Appeals. We sincerely believe that the petition for Writ of Certiorari fails to present any reason for a review of this case by this Court.

Respectfully submitted,

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AUG 13 1945
CHARLES ELMORE CROPLEY

IN THE

Supreme Court of the United States

OCTOBER TERM, 1944.

No. 164 + 165

LORRAINE CASTLE APARTMENTS BUILDING CORPORATION, INC., ET AL.,

Petitioners,

vs.

JUSTIN MACKIEWICH, ET AL.,

Respondents.

ANGELO CASTELLANI, ET AL.,

Petitioners,

vs.

JAMES W. McNICHOLS, TRUSTEE, ET AL.,

Respondents.

REPLY OF WILLIAM BART, INTERVENING PETITIONER, IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI.

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Respondents.

REPLY OF WILLIAM BART, INTERVENING PETITIONER, IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI.

STATEMENT OF THE CASE.

The action is a Chapter 10 proceedings brought by a corporation which is the owner of an apartment building located in the City of Chicago, Illinois, at 5001 West Monroe

Street, consisting of twenty-four (24) apartments, constructed in the year 1928, and having an annual income of approximately Fourteen Thousand, Eight Hundred ($14,800.00) Dollars (Tr. 123).

The petition was filed on the 30th day of April A. D. 1942 (Tr. 2), and was approved as filed in good faith on the 5th day of May, 1942 (Tr. 11). In 1935, the debtor corporation filed a 77 B proceedings which culminated in a seven (7) year extension, thereby extending the maturity date to April 30, 1942 (Tr. 52).

The petition filed by the debtor corporation on April 30, 1942, provided among other things, that the payment of the bonds be extended for a period of five (5) years; that the debtor continue to pay interest on all outstanding bonds and continue the retirement of the bonds by purchase from time to time through the sinking fund Tr. 5).

On the 12th day of August, 1942, the debtor corporation filed a plan of reorganization which, in sum and substance, provided that the bondholders receive seventy (70%) per cent of the face value of their bonds (Tr. 23); that the debtor borrow Fifty Thousand ($50,000.00) Dollars, and use the cash on hand in the sum of Four Thousand Forty-nine and Ninety-four ($4,049.94) Cents on deposit at the First National Bank in Chicago, Illinois, towards the payment of Seventy (70¢) cents on the dollar to the bondholders plus expenses of reorganization (Tr. 22).

On October 6, 1942, Archie H. Cohen, Referee in Bankruptcy as Special Master, filed a report with the Clerk of the Court and recommended the disapproval of the debtor's plan of reorganization as being unfair and inequitable (Tr. 30). On October 22, 1942, leave was granted to the debtor by the Referee to amend the plan of reorganizaton, the amendment providing for the payment of eighty (80%) per cent of the face value of the bonds instead of seventy (70%) per cent (Tr. 33 and 34).

On January 15, 1943, the Referee in Bankruptcy as Special Master filed a supplemental report, on the amended plan and recommended that the amended plan be disapproved since the offer of eighty (80¢) cents on the dollar was not fair and reasonable (Tr. 65). On July 20, 1943, the Court having the case under advisement pursuant to Rule 7, removed the debtor corporation from possession and appointed James W. Nichols as Trustee, and directed the Trustee to prepare a plan of reorganization embracing the sale of the property if fair and feasible and directed that the same be submitted before the Special Master (Tr. 92).

On the 7th day of September, 1943, the Trustee filed a plan of reorganization which provided for the sale of the property at an upset price of Seventy-five Thousand ($75,000.00) Dollars (Tr. 126 and 123). On the 15th day of September, 1943, the debtor asked for leave to withdraw the last plan of reorganization submitted and for leave to file an amended plan of reorganization which provided that the principal stockholder contribute Ten Thousand ($10,000.00) Dollars in addition to the funds now on hand in the bank account of the Trustee in bankruptcy to pay the bondholders accrued interest to date and a cash dividend (Tr. 36). The debtor's plan further provided that the time of payment be extended for five (5) years with interest at five (5%) per cent per annum and that the claims of persons that have acquired bonds during the pendency of these proceedings, namely $52,500.00 out of the total issue of $72,500.00, be limited to the amount paid therefor.

The Referee as Special Master on October 7, 1943 filed a report upon the plan of reorganization submitted by the Trustee upon the amended plan of reorganization filed by the Debtor (Tr. 147). In his report, the Referee as Special Master recommended that the amended plan of

reorganization of the debtor be disapproved as being unfair and unfeasible (Tr. 162). The Referee as Special Master, also recommended that the Trustee's plan of reorganization to sell at an upset price of Seventy-Five Thousand ($75,000.00) Dollars be approved, as fair and feasible (Tr. 163).

The Special Master, further recommended that the claims of persons that purchased bonds during the pendency of these proceedings, be allowed on a parity with other claims, since no privity existed between the purchaser of the bonds during the pendency of the proceedings and that of the Debtor and that no fraud was committed by those who purchased bonds during the pendency of this proceedings (Tr. 161).

On November 1, 1943, the Debtor, its stockholders and a purported bondholder filed a motion requesting that the court limit the claims of persons that purchased bonds during the pendency of the proceedings. The Court took the motion under advisement and considered it along with objections filed to the plan (Tr. 405).

On February 10, 1944, the Court entered an order, granting the Debtor leave to file a petition, to limit the allowance of certain claims and denied said petition, stating that no new issues had been raised apart from the fully considered objections to the Trustees' plan (Tr. 451).

On the 21st day of February, 1944, the Court entered an order, approving the plan of reorganization of the Trustees, in accordance with the memorandum of February 10, 1944 (Tr. 457).

On the 10th day of March, 1944, the Debtor filed a notice of appeal from the order of February 10, 1944 denying Debtor's petition to limit the claims of certain bondholders (Tr. 461).

On the 20th day of March, 1944, Angelo Castellani and Margaret Castellani, the purported stockholders of the Debtor, filed a petition in the District Court to dismiss the proceedings for want of jurisdiction, since the corporation had been dissolved by a decree entered June 18, 1935, in the Superior Court of Cook County.

On the 21st day of March, 1944, Angelo Castellani and Margaret Castellani filed a notice of appeal, from the order entered on the 21st day of February, 1944, approving the report of the Special Master, filed on October 7, 1943, approving the plan of reorganization filed by the Trustee, and overruling the objections to the Report of the Special Master.

The Circuit Court of Appeals rendered a decision on the 4th day of May, 1945, (Rec. 503) affirming the decree of the District Court entered on the 10th day of February, 1944, denying debtor's petition to limit the claims of certain bondholders (Tr. 494) and affirming the plan of reorganization of the Trustees in accordance with the memorandum of the District Court on February 10, 1944 (Tr. 494).

PROPOSITIONS OF LAW RELIED ON.

I.

The Supreme Court of the United States will not attempt to analyze evidence where both the District Court and the Circuit Court of Appeals have concurred in findings of fact.

Workman v. *New York*, 179 U. S. 552.
Schwartz v. *Duss*, 187 U. S. 8.
Wilderoft, 201 U. S. 378.
Bochmer v. *Pennsylvania Railroad Co.*, 252 U. S. 496.
Page v. *Arkansas N. G. Corp.*, 286 U. S. 269.
Pick Manufacturing Co. v. *General Motors Corporation*, 299 U. S. 3.
Virginia Railroad Co. v. *System Federation #40*, 300 U. S. 515.

II.

No dispute exists between different circuits.

III.

No new question has been presented which has not been decided previously.

Country Life Apartments, Inc. v. *Buckley*, 145 Fed. (2d) 934 (C. C. A. 2nd 1944).
In re V. Loewer's Gambrinus Brewery Co., Inc., 141 Fed. 2d 747 (C. C. A. 2d, 1944).

ARGUMENT AND BRIEF.

The Supreme Court of the United States will not attempt to analyze evidence where both the District Court and the Circuit Court of Appeals have concurred in the findings of fact.

May it please the Court the Debtor corporation has attempted to invoke the jurisdiction of this court under Section 240 of the Judicial Act as amended, 28 U. S. A. 347. The debtor sets forth under the title "Questions Presented" four items as the basis for the issuance of a Writ of Certiorari which are as follows:

> "1. While the Court in a Chapter X proceeding is in the process of working out a plan agreeable to the debtor and more than two-thirds of its creditors, is interference by speculators who connive and conspire to solicit and buy up more than two-thirds of debtor's bonds while the debtor's hands are tied, with the object of preventing reorganization and forcing liquidation, a violation of Chapter X of the Bankruptcy Act.
>
> 2. Under such circumstances should the Court have summarily denied the petition to restrict claims so purchased to the amount paid for them.
>
> 3. Under such circumstances should the Court have refused to submit to the creditors the debtor's proposal to contribute additional funds, make immediate distribution of a substantial amount, pay the balance of all claims in full in five years, with interest at 5%, or if such claims were so limited, to make immediate payment of all claims in full.
>
> 4. Under such circumstances does Chapter X of the Bankruptcy Act upon a voluntary petition for reorganization, permit liquidation under the guise of reorganization, without an adjudication in ordinary bankruptcy."

The debtor then takes the above mentioned statements which it presents as questions to be decided by this court as a basis or reason for the allowance of the Writ of Certiorari. The debtor says that the following questions should be settled by this Court:

1. "Is the solicitation by speculators of a debtor's bonds during the pendency of a reorganization proceeding under Chapter X of the Bankruptcy Act *for the purpose of preventing a reorganization* prohibited by the Act of general equitable principles, or is it to be sanctioned in order not to 'destroy or impair the sales value of securities by abolishing the profit motive which inspires purchasers' ".

2. "The Statute does not contemplate a liquidation in a Chapter X proceeding, but a liquidation in ordinary bankruptcy, or a dismissal outright."

The debtor, under the heading "Errors relied upon", once again rewords and rehashes the items stated under the headings "Questions Presented" and "Reasons Relied Upon for the Writ of Certiorari", and, in substance says that the Court erred in refusing to limit the participation of those who purchased their bonds during the pendency of the proceedings; that the District Court should have permitted a full hearing on the petition to limit the participation of certain bondholders; that the Court should have approved an extension for five (5) years as requested by the debtor; and that the Court should not permit "liquidation under the guise of reorganization".

The debtor under the guise of having this Court determine whether speculation in bonds bought and sold during the pendency of the proceedings should be permitted, attempts to have this Court consider the merits of the debtor's plan of reorganization and its plea to limit

the participation of those who purchased their bonds during the pendency of the proceedings.

Regardless of whether or not this Court feels speculation in bonds after a petition is filed under Chapter X should or should not be permitted, is of no consequence in this case. Assuming merely *arguendo* that under certain circumstances a limitation should appropriately apply as in a case where fraud was committed or the parties acted in a fiduciary capacity, those circumstances do not exist here. The debtor failed to prove that there was any fraud in the purchase of bonds made by purchasers during the pendency of the proceedings; that there was any fiduciary relationship between the purchasers of the bonds and other members of the corporation or the other bondholders; or, that the bonds were purchased for the purpose of preventing a reorganization. The Master found that no fraud was committed in the purchase of the bonds and both the District Court and the Circuit Court of Appeals concurred in these findings.

It has become a universal rule that Courts will not interfere and limit the holders of securities purchased during the pendency of reorganization proceedings to the amount paid therefor unless fraud was created or if the purchasers of the bonds acted in a fiduciary capacity.

Mokova Corporation v. *Dolan*, 147 F. 2d 340. The theory of the Courts in refusing to limit participation of claimants to the amount paid therefor, except in unusual circumstances, is that the value of any claim would be zero if the purchaser could receive no more than he paid therefor.

A debtor corporation by following the tactics and procrastinations of the debtor corporation in the case at bar could virtually compel the holders of claims to accept any form of plan of reorganization, since they could not sell

their claims during the pendency of the proceedings and by procrastination could continue the litigation indefinitely. In fact, such a ruling would tend to affect the marketability of securities of this corporation that are even in good standing, since the filing of a Chapter X proceeding by any corporation, would cause the value of its securities that it issued to become frozen in the hands of the general public. Many investors would be very reluctant to loan money on this basis.

This Court has held in a number of cases, *Workman* v. *New York*, 179 U. S. 552; *Schwartz* v. *Duss*, 187 U. S. 8 and *Wildcroft*, 201 U. S. 378 that where both courts below have concurred in a finding of fact, it will be accepted as conclusive unless it affirmatively appears that the lower courts obviously have erred. In *Boehmer* v. *Pennsylvania Railroad Co.*, 252 U. S. 496, the Court said where two courts have agreed as to construction to be placed upon certain facts, the Supreme Court will not enter into a minute analysis of the evidence. *Page* v. *Arkansas N. G. Corp.*, 286 U. S. 269, *Pick Mfg. Co.* v. *General Motors Corporation*, 299 U. S. 3, *Virginia Railroad Co.* v. *System Federation # 40*, 300 U. S. 515.

The debtor contends that the District Court erred in denying its petition for a limitation of the claims purchased during the pendency of the proceedings. The debtor assumes in its argument that it is an established fact that the claim holders (bondholders) purchased the claims for the purpose of preventing the approval of the plan of reorganization. The debtor has made allegations and conclusions of fraud, but has never been able to introduce any proof to support them. The petition to which the debtor has reference was filed on November 1, 1943, approximately over a year after a hearing was held on the identical question of the limitation of the claims of bondholders who purchased their bonds during the pendency

of the proceedings (Rec. 169). If the Court would permit the continual filing of petitions for the adjudication of questions which have been once adjudicated, proceedings such as these could never be culminated. The result being, as previously stated, that bondholders would be forced to accept any plan offered by the debtor regardless of whether it was fair and equitable to all claimants.

The debtor claims error was committed by the District Court in its failure to decide that an extension for five (5) years was fair and feasible. Whether such a plan was fair and feasible is a question of fact. The Master found that an extension was not fair and feasible, the District Court and the Circuit Court of Appeals have concurred. As previously stated, this Court has always taken the position that it will not review questions of fact.

No dispute exists between different circuits.

No new question has been presented which has not been decided previously. The debtor further contends that error was committed by the District Court and the Circuit Court of Appeals in approving a plan of reorganization which embodied a liquidation of the assets of the corporation. The debtor has set this item up as question number 4 to be decided by this Court.

This Court, in the decisions rendered over a period of years, has set a basis upon which it will assume jurisdiction: (1) that a dispute exists between different circuits; (2) that a new and novel question has been presented and the Circuit Court of Appeals has no guiding post.

This case involves neither of the two points which should act as a basis for this court in assuming jurisdiction.

The Circuit Court of Appeals, Second Circuit, in the case of *Country Life Apartments* v. *Buckley*, 145 Fed. (2nd) 934, has concurred in the decision of the Lorraine

Castle Apartments Building Corporation, citing the case expressly in its opinion on Page 938:

> "Here when the petition was filed it did not appear that the debtor had no chance for reorganization or that reorganization would not be a reasonable method of serving the best interests of creditors and stockholders. The District Court found that the petition was filed in good faith, and that order was never appealed from. It cannot now be attacked for lack of jurisdiction. Bankruptcy Act, § 149. The course of proceedings indicates also the good faith of the attempts to reorganize. * * *
>
> "Under these circumstances *Fidelity Assurance Ass'n* v. *Sims, supra,* does not apply, and the trustee's plan was properly approved and confirmed by the District Court as being within the language of Bankruptcy Act, § 216(10), which provides that a plan of reorganization may include the sale of all or any part of the debtor's property at a fair upset price and the distribution of all or any assets among those having an interest therein. This conclusion is amply supported by our own decisions and those of other courts. *In re V. Loewer's Gambrinus Brewery Co.*, 2 Cir., 141 F. (2nd) 747; *In re Lorraine Castle Apartments Bldg. Corp.*, D. C. N. D. Ill., 53 F. Supp. 994. See also *In re Central Funding Corp.*, 2 Cir., 75 F. 2nd 256, and *In re Porto Rican American Tobacco Co.*, 2 Cir., 112 F. 2nd, 655, both of which were distinguished and not disapproved in *Fidelity Assurance Ass'n* v. *Sims, supra.*"

The debtor has drawn a conclusion that the intervening petitioner, Bart, who purchased the $52,000.00 bonds, conspired to prevent a reorganization and thereby force liquidation. Whereas, the facts show that the intervening petitioner did not conspire with any one and did not attempt to prevent a reorganization. The attorney for the debtor appeared before the District Court judge in October of 1942, at the time the Master recommended that

the debtor pay 85¢ on the dollar for the outstanding bonds, and represented to the court that bondholders were selling their bonds at 70¢ on the dollar and up (Rec. 218). The debtor's attorney then requested "that your Honor also direct the Referee and Special Master to make such investigation as may seem advisable with respect to what is going on in the purchase of these bonds as I have indicated" (Rec. 218).

That hearing took place on October 15, 1942 and as a result thereof an order of reference for the purpose of investigating the purchase of the bonds was made. (Rec. 32).

The Special Master after conducting lengthy hearings from October 15, 1942 until January of 1943 filed a Supplemental Report (Rec. 64) in which he said that there was no attempt to perpetrate a fraud upon the court by the purchaser of the bonds.

The District Court in its opinion, 42 Fed. Supp. 973 (Rec. 449) said:

> "With reference to the acquisition of $52,000 of bonds by 'speculators' during the pendency of the proceedings, the Special Master has found that there was no fraud involved in the purchase of these bonds and that the purchasers are not and never were in a fiduciary relationship with the bondholders, the debtor, or stockholders of the debtor. The evidence in this case does not warrant disturbing the findings of the Special Master on these two points, and, as there is no proof that the bonds in question have been acquired by their present owners for the purpose of accepting or rejecting a plan other than in good faith, this Court is not disposed to disqualify these bonds from voting upon the plan of reorganization approved herein."

The debtor by mere allegation has attempted to convince the District Court, the Circuit Court of Appeal and

this court that the purchaser of $52,000 in bonds created a fraud on the other bondholders, whereas the Master, the District Court Judge and the Circuit Court of Appeals found that no fraud was committed, and that there was no basis to limit the participation of the intervening petitioner, Bart.

The Circuit Court of Appeals in its decision (Rec. 498) says:

> "Under the order of reference, the special master had jurisdiction of the parties and of the subject matter and heard fully all the evidence relating to alleged fraud upon the part of the so-called speculators. He saw the witnesses, observed them upon the witness stand and made his findings and these the court approved. Indeed the evidence offered by the debtor and its stockholders failed utterly to establish any possible fraud upon the corporation or any of the beneficiaries of the estate.
>
> "The debtor's obligation is to pay his debts. The property right of a bondholder is the right to receive from the debtor the entire amount the latter has promised to pay. In the absence of some equitable reason, taking the case out of the ordinary rule, the prices which security holders pay for their securities in no wise affects the measure of their participation in reorganization or their voting power. *Security-First Natl. Bank* v. *Rindge Land & Navigation Co.*, 85 F. 2nd, 557, 561 (CCA9): *In re Utilities Light & Power Corp.*, 29 F. Supp. 763, 770; *Standard Gas & Electric Co.* v. *Deep Rock Oil Corp.*, 117 F. 2d, 615, 619 (CCA10) cert. den. 313 U. S. 564; *Mokava Corporation* v. *Dolan*, ... F. 2d ..... (CCA2), January 2, 1945. To reduce the participation to the amount paid for securities, in the absence of exceptional circumstances which are not present here, would reduce the value of such bonds to those who have them and want to sell them. This would result in unearned, undeserved profit for the debtor, destroy or impair the sales value of securities by abolishing the profit mo-

tive, which inspires purchasers. This is even more evident when the purchaser acquires a lawsuit when he buys a debt. He hopes to realize more than he pays and at the same time runs the risk of recovering less. If the claimants are limited to the amounts paid, the debtor will never offer to bondholders anything above the current price for the bonds. This would encourage the debtor to delay the plan for rehabilitation in the hope that he will be able to settle the claims against him at less than a fair amount. Such results are not in accord with the purposes of the legislation. *Security-First Natl. Bank* v. *Rindge Land & Navigation Co.*, 85 F. 2d. 557, 563 (CCA9); *Mokava Corporation* v. *Dolan*, ... F. 2d ..... (CCA2), January 2, 1945. We conclude that there is no basis upon which we could sustain any objection to the finding of fact that the claims of bondholders are without fraud. Accordingly, the order entered was entirely proper.

"But appellants argue that they have not had their day in court; that they filed a petition which the court dismissed without hearing. If this were a fact, of course, their complaint would be well founded. But the record discloses that the court had already made an adjudication of the issues involved before this petition was filed. That petition presented no question which had not previously been fully considered by the master at the hearing on the trustee's plan and objections thereto. Thus the trustee's plan provided for no limitation upon the claims for any bondholder. Among the objections interposed by appellants was one that the claims were fraudulent and should be limited to the amounts paid and that they be specifically held not entitled to vote on any plan. The issue was drawn, evidence presented, and a decision made. When the court approved the master's report in this respect, he completely adjudicated all the issues raised and presented by the petition. Therefore, it was properly denied.

"Appellant insists that a plan of reorganization may not properly contemplate a sale of the debtor's property. Section 216 (10) of the Bankruptcy Act, (11

> U. S. C. A., Sec. 616 (10)), provides that a plan of reorganization 'shall provide adequate means for the execution of the plan,' which may include: the retention by the debtor of all or any part of its property; the sale or transfer of all or any part of its property to one or more other corporations theretofore organized or thereafter to be organized; the merger or consolidation of the debtor with one or more other corporations; the sale of all or any part of its property, either subject to or free from any lien, at not less than a fair upset price and the distribution of all or any assets, or the proceeds derived from the sale thereof, among those having an interest therein."

The Debtor has attempted by insinuation and implication to convince this court of a direct falsehood that the owner and holder of $52,000 in bonds was committing a fraud upon this court. The entire proceedings and the request for this court to take jurisdiction resolves itself into the definite conclusion that the instant case is one where a disgruntled debtor is attempting to use his right of appeal merely for the purpose of delay and of causing untold expense to the bankrupt estate.

The Debtor has attempted to use the decisions of *American Insurance Co.* v. *Avon Park*, 311 U. S. 138 as a basis for limiting the claims of purchasers of bonds during the pendency of the proceedings. In the *Avon Park* case, the parties were in a fiduciary capacity which situation did not prevail in the instant case, and therefore that decision does not apply.

In the case of *Equitable Reserve Assn.* v. *Dardanelle Special School District*, 138 Fed. (2nd) 236 in which case the appellants complained that the plan was inequitable and discriminatory against Rainey & Sons who had paid $61,908 for a $121,000 claim and would receive a larger percentage of the cost than would the appellants who were original bondholders, the Court pointed out expressly that

the City of Avon Park, *supra* does not support the contention for the limitation of bondholders who purchase their bonds during the pendency of the proceedings.

The debtor also cities *Case* v. *Los Angeles Lbr. Co.*, 60 Supreme Court, 1, that the purpose of Sec. 77-B is to avoid liquidations and force sales with drastic deflationary effects.

We are now operating under Chapter X proceedings and the *Country Life* case *supra* is further basis for the approval of the Circuit Court of Appeals' decision in the case at bar.

The only basis which the debtor can find to support its contention that a liquidation should not be permitted under a Chapter X proceedings is the case of *Fidelity Assurance Association* v. *Sims*, 318 U. S. 608 (1943). That case has been distinguished from the case at bar and that of the *Country Life Apartments, Inc.* v. *Buckley*, 145 F. 2d 935 (C. C. A. 1944). The Sims case stands for the proposition that a Chapter X proceedings should be dismissed if it cannot meet the statutory requirements of having been filed in good faith and where at the outset the only solution would be a liquidation similar to a regular bankruptcy liquidation. In the case at bar, the petition was approved as having been filed in good faith in May of 1942, said order was never contested or appealed from by the debtor and that order must stand.

It cannot be said that a sale was contemplated in the first instance in the case at bar when the Chapter X proceedings was filed. It was only after the continued delay and procrastination of the debtor, and the recent real estate market which convinced all those concerned that if the property was sold today, all claimants could be paid one hundred cents on the dollar plus accrued interest to date at the rate of seven (7%) per cent, and at the same time leave a substantial sum for the debtor.

One cannot help but remember that the debtor after filing his petition and having it approved as being filed in good faith, offered to pay but seventy cents on the dollar using the funds on hand to make such payment and now feels dissatisfied and disgruntled because all of the creditors will receive one hundred cents on the dollar, plus interest, and the debtor will receive a substantial sum for his equity, whereas if the original plan proposed by the debtor had been successful, the debtor would have made additional profit.

The debtor has attempted to put a new color on his petition for limitation of purchasers of bonds during the pendency of the proceedings by having a bondholder join in the petition. The bondholder under the Trustee's plan receives one hundred cents on the dollar, plus seven (7%) per cent interest, in accordance with the terms of the Trust Deed, and, therefore, does not have an appealable interest. Counsel for the intervening petitioner stated that fact to be before the Circuit Court of Appeals in his brief, but the Circuit Court of Appeals found it unnecessary to consider the point inasmuch as the point approved the Trustee's plan of reorganization.

Conclusion.

The reasons that impelled the District Court to approve the Trustee's plan of reorganization and to deny the debtor's petition to limit the claims of those who purchased bonds during the pendency of the proceedings and that of the Circuit Court of Appeals in affirming the orders of the District Court have now become obvious from the facts as shown in our brief.

1. The Supreme Court of the United States will not attempt to analyze evidence where both the District Court and the Circuit Court of Appeals have concurred in findings of fact.

2. No dispute exists between different circuits.

3. No new question has been presented which has not been decided previously.

We respectfully submit that these reasons amply justify this Court in affirming the decisions of the District Court and the Circuit Court of Appeals.

Respectfully submitted,

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